

VZCZCXR05856

RR RUEHBI RUEHCI RUEHDBU RUEHFL RUEHKW RUEHLA RUEHLH RUEHNEH RUEHNP
RUEHPW RUEHROV RUEHSL RUEHSR
DE RUEHTA #2005/01 3161017
ZNY CCCCC ZZH
R 121017Z NOV 09
FM AMEMBASSY ASTANA
TO RUEHC/SECSTATE WASHDC 6811
INFO RUCNCLS/ALL SOUTH AND CENTRAL ASIA COLLECTIVE
RUCNCIS/CIS COLLECTIVE 2143
RUEHZL/EUROPEAN POLITICAL COLLECTIVE
RUEHBJ/AMEMBASSY BEIJING 1513
RUEHUL/AMEMBASSY SEOUL 1148
RUEHKO/AMEMBASSY TOKYO 2214
RUEHAK/AMEMBASSY ANKARA 2218
RHMFIISS/CDR USCENTCOM MACDILL AFB FL
RUEAAIA/CIA WASHDC
RUCPDOC/DEPT OF COMMERCE WASHINGTON DC
RHMFIISS/DEPT OF ENERGY WASHINGTON DC
RUEATRS/DEPT OF TREASURY WASHINGTON DC
RHEFAAA/DIA WASHDC
RHEHNSC/NSC WASHDC 1703
RUEKJCS/JOINT STAFF WASHDC
RUEKJCS/SECDEF WASHDC 1561

C O N F I D E N T I A L SECTION 01 OF 04 ASTANA 002005

SIPDIS

STATE FOR SCA/CEN, S/EEE, S/CIEA, EEB

E.O. 12958: DECL: 03/06/2059

TAGS: PGOV PREL ECON EINV EPET RS TX KZ

SUBJECT: KAZAKHSTAN: CHEVRON CEO DISCUSSES MEETINGS WITH NAZARBAYEV, BERDIMUHAMEDOV

REF: A. ASTANA 1105

1B. ASHGABAT 1353

Classified By: Ambassador Richard E. Hoagland, 1.4 (b), (d)

11. (C) SUMMARY: Chevron's current and incoming CEOs, Dave O'Reilly and John Watson, briefed the Ambassador on November 11, following their meeting earlier that day with President Nazarbayev. Jay Johnson, Director of Chevron's Eurasia Business Unit, and amira Kanapianova, Country Director for Kazakhstan, also attended the early-evening briefing at the Ambassador's residence. Chevron's meeting with Nazarbayev covered production and local content at Tengizchevroil (TCO), economic diversification, fines and fees for allegedly improper sulfur storage, and oil transportation issues, including expansion of the Caspian Pipeline Consortium (CPC) pipeline. According to O'Reilly, Kazakhstan's Supreme Court ruled on November 11 that TCO does not have to pay \$310 million in administrative fees assessed on top of a \$342 million fine for allegedly improper sulfur storage. O'Reilly said Chevron is now focused on executing an agreement he personally negotiated with Nazarbayev in June to drop the sulfur fines and fees. Watson briefed the Ambassador on Chevron's plans in Turkmenistan and gave a readout of his meeting in April with Turkmenistan President Berdimuhamedov, who Watson said understands that Turkmenistan needs outside expertise to develop its complex onshore oil and gas fields.
END SUMMARY.

NO CEO FOR LIFE

12. (C) O'Reilly told the Ambassador that the purpose of the meeting with Nazarbayev was to introduce his successor, John Watson, who will become Chevron's CEO on January 1, 2010. He said he and Nazarbayev, whom he has known for more than a decade, spent some of their meeting reminiscing about the early days of Tengiz exploration and production. According to O'Reilly, Nazarbayev seemed "a little tired," but was in good spirits and had a firm handshake. He said that Nazarbayev was very pleased with TCO's performance and investment in local content. (NOTE: TCO is Kazakhstan's largest oil producer at 24 metric tons a year, or 600,000

barrels per day. In 2009, TCO paid \$4 billion to the government in taxes and royalties and spent another \$1 billion with local, Kazakhstani contractors. END NOTE). Nazarbayev stressed the importance of technology and economic diversification, which will be the theme of the next Foreign Investors' Council in December, and encouraged Chevron to continue its planned construction of a polyethelyne production plant in Atyrau oblast.

SUPREME COURT OVERTURNS ADMINISTRATIVE PENALTY

¶3. (C) When asked about reports that TCO may be assessed more than \$1 billion in fines and fees for allegedly improper sulfur storage, O'Reilly told the Ambassador that he had good news to report. On November 11, Kazakhstan's Supreme Court overturned a ruling from a lower court, which charged TCO an administrative penalty of \$310 million in addition to a \$342 million fine. O'Reilly said that he reminded the president during their meeting of their gentlemen's agreement on the sulfur issue reached while playing a private game of golf in June (reftel A). Nazarbayev, according to O'Reilly, instantly recalled the precise details of the agreement, while the Ministers at the meeting nodded in concurrence. "His memory is still very good," said O'Reilly. "He replayed our agreement, word for word." Johnson mentioned that all relevant ministries -- the Ministry of Finance, the Ministry of Energy and Mineral Resources, and the Ministry of Environmental Protection -- have consented to abide by the agreement, and Chevron is now working to bring the General Prosecutor's Office on board. Johnson said Chevron hopes to have the agreement executed as

ASTANA 00002005 002 OF 004

early as next week. Johnson admitted that the government informed TCO General Director Todd Levy on November 6 that it would assess an additional \$800 million fine on TCO for improper sulfur storage (reftel), but he said TCO has not yet been formally served notice. He expressed hope that if the government agrees to drop the pending charges, it will not pursue the new case.

CPC EXPANSION LIKELY IN 2010

¶4. (C) Chevron's senior executives also discussed oil transportation issues with Nazarbayev, including CPC expansion and the Kazakhstan Caspian Transportation System (KCTS). According to O'Reilly, "we're getting close -- ok, closer -- to an agreement on CPC expansion." He said Chevron is still pushing for an agreement by the end of the year but, privately, told the Ambassador that they would be satisfied with a full and final agreement by the third quarter of 2010.

Johnson asserted that the CPC consortium has agreed that national oil company KazMunaiGas (KMG) will manage expansion activities in Kazakhstan, while Russia's state-owned oil transportation company Transneft, currently the largest CPC shareholder with 31%, will manage the work inside Russia. Chevron will manage the expansion of the terminal in Novorossiysk.

¶5. (C) Johnson explained the two stages to CPC expansion: (1) reach agreement with shareholders on ship-or-pay contracts, the project budget, the sources of funding, etc.; and (2) select a technical proposal from competitive bids, and sanction the expansion project. Johnson highlighted the time necessary to prepare bid packages for the engineering work, and declared Chevron will be patient with the process, with the expectation that shareholders will vote to sanction the expansion no later than the third quarter of 2010. When asked to comment on the Russian government's views of CPC expansion, O'Reilly said that Nikolai Tokarev, Transneft's CEO, and Deputy Prime Minister Igor Sechin have both expressed support for the project. According to O'Reilly, Transneft CEO Tokarev personally assured him of his support for CPC expansion during a meeting in Moscow this year, while Sechin cited CPC expansion as one of the government's top energy priorities during a June 2008 conference in St.

Petersburg. On KCTS, O'Reilly asserted KMG's continued insistence on control of the Eskene-Kuryk pipeline, while KMG and the State Oil Company of the Azerbaijan Republic (SOCAR) will own and manage the trans-Caspian portion of the project.

SAMSUN-CEYHAN PIPELINE

¶6. (C) O'Reilly said that Nazarbayev emphasized the importance for Kazakhstan of developing multiple oil export routes, a point he has made during all of their previous meetings. For example, Nazarbayev told O'Reilly that during his October 22 visit to Turkey, Kazakhstan offered to participate, jointly with Russia, in the construction of the Samsun-Ceyhan oil pipeline. According to O'Reilly, Nazarbayev made clear that this is a very long-term issue for Kazakhstan but is not an immediate priority of the president's. (NOTE: The 340-mile pipeline would have a capacity of 1.5 million barrels per day -- larger than the current capacity of the Baku-Tbilisi-Ceyhan pipeline. The pipeline project company is 50% owned by Turkey's Calik and Italy's ENI, which also owns 16.81% of Kazakhstan's Kashagan oil fields. END NOTE).

PIPELINES TO CHINA

¶7. (C) Nazarbayev also told O'Reilly that Kazakhstan considers the oil and gas pipelines to China strategically important, particularly the Beineu-Bozoi segment of the gas pipeline, which will enable Kazakhstan to avoid gas transit shipments via Uzbekistan and increase its energy security.

ASTANA 00002005 003 OF 004

"Nazarbayev really does not like being dependent on Uzbekistan" for gas or electricity, O'Reilly highlighted. Watson added that Kazakhstan has serious plans to develop the domestic gas market, including construction of a 150 megawatt, gas-fired power plant to supply power to Almaty and Shymkent. O'Reilly said Nazarbayev told him that China's President Hu Jintao will visit Kazakhstan in December for a ribbon-cutting ceremony to inaugurate the gas pipeline. When asked if the gas pipeline would be completed by then, O'Reilly joked, "Since when do you need a completed project in order to have a ribbon-cutting ceremony?" When queried if Chevron could envision a scenario under which it would ship crude from Tengiz eastward to China, O'Reilly answered, "Yes. China is deficit in oil, especially in its western regions, and is increasing its refining capacity in the west. The new fields, which they are exploring there, appear mainly to be rich in gas, not oil. If they are willing to pay a commercial price, then yes, we would ship to China." Johnson added that Chevron's decision would be influenced by the available transportation options: if, for example, there is no agreement to expand the CPC pipeline, and KCTS continues to be stalled, the eastern route would be more attractive to Chevron.

TURKMENISTAN KNOWS IT NEEDS HELP

¶8. (C) The Ambassador asked about Chevron's plans and prospects in Turkmenistan. Both O'Reilly and Watson were cautiously optimistic, noting that Chevron has submitted a number of proposals awaiting government action. Watson, who met with Turkmenistan's President Berdimuhamedov shortly after the gas pipeline explosion in April, confirmed Chevron's intentions to take over management of a gas processing contract from Gazprom (reftel B). Watson highlighted Chevron's good relationship with Berdimuhamedov ("We believe we have a preferred relationship.") and added, "He knows that he needs help. He knows what his people can, and cannot, do." When pressed to say whether he truly believes that Berdimuhamedov recognizes that Turkmenistan cannot develop its complex onshore fields without Western assistance, Watson stood firm. "I believe he understands this. He told me directly, in a private conversation. I was terribly impressed by his technical knowledge and command of the issues." Watson said Berdimuhamedov advised Chevron to

be patient, and he speculated that Berdimuhamedov is trying to build domestic political support for a more open policy toward foreign investment in the oil and gas sector. "Internally, politically, he needs time to achieve alignment" for his policies, Watson explained. When asked how much Berdimuhamedov trusted other senior officials, Watson replied, "I don't really know. They are coming out of a long, dark period, and there is not much trust in Turkmenistan. I will say this: when we met, it was just him, me, our Vice President for Business Development, and a 28-year old interpreter." Watson also reported that Berdimuhamedov is not always given accurate information about Western companies or Western governments. He suspected that Russian propaganda and disinformation is to blame. "The day we arrived," for example, "there were rumors of a coup in the capital. During an oil and gas conference!"

NAZARBAYEV LOOKING FORWARD TO APRIL NUCLEAR SUMMIT

¶9. (C) O'Reilly told the Ambassador that during his June meeting with Nazarbayev in Astana, Nazarbayev mentioned that he was very pleased to have received a phone call from Vice President Biden, inviting him to attend the April 2010 Global Nuclear Security Summit in Washington. O'Reilly highlighted the importance of nuclear non-proliferation to Nazarbayev personally, and that he is very much looking forward to his visit to Washington.

¶10. (C) COMMENT: Chevron's candid comments confirm several

ASTANA 00002005 004 OF 004

fundamental facts about doing business in Kazakhstan. First, President Nazarbayev remains firmly in charge. He is the decider, on issues as strategically significant as the development of new oil export pipelines, or as mundane as administrative penalties for sulfur storage. Implementation of informal, gentlemen's agreements will always be tricky in a place like Kazakhstan, but unfortunately, that is still how the most important decisions are made: through personal, private negotiations with the president. Second, the briefing underscores the strategic success -- and existential importance -- of Kazakhstan's "multi-vector" policy. Nazarbayev knows that he needs the China pipeline and trans-Caspian crossing as much as the Russian route. So far, he has demonstrated the political savvy, negotiating skills, and tactical flexibility necessary to keep all paths out of this land-locked country open and unfettered. Third, Chevron's meeting with Nazarbayev and the continued growth of Tengizchevroil confirm that U.S. companies can be extremely successful in Kazakhstan -- but even the most high-profile, preferred investors must make major investments to develop local capacity and achieve economic diversification if they are to remain in the president's good graces. END COMMENT.

HOAGLAND